

Modification proposal:	Uniform Network Code (UNC) 857: Revision to the Determination of Non-Transmission Services Gas Year Target Revenue (UNC 857)
Decision:	The Authority ¹ directs this modification be made ²
Target audience:	UNC Panel, Parties to the UNC and other interested parties
Date of publication:	19 April 2024
Implementation date:	To be confirmed by the code administrator

Background

National Gas Transmission (NGT) recover their System Operator Allowed Revenue³ through General Non-Transmission Services (GNTS) charges: a commodity charge levied on gas flowed by Users through the National Transmission System (NTS). Under the terms of their license, NGT is entitled to recover specified Allowed Revenue over a Formula Year (April to March). As the tariff year under the UNC is over the course of a Gas Year (October to September), there is a requirement for NGT to calculate a target revenue for the Gas Year which coincides with the two 'part' Formula Years.

The misalignment between the Formula Year and Gas Year can contribute towards large swings in GNTS charges should NGT's Allowed Revenue change significantly. The onset of the wholesale gas crisis in 2021 greatly increased the cost for NGT of procuring shrinkage gas needed to operate the NTS. These increased costs have since flowed through into volatile year-on-year GNTS charges for Users.

¹ References to the "Authority", "Ofgem", "we" and "our" are used interchangeably in this document. The Authority refers to GEMA, the Gas and Electricity Markets Authority. The Office of Gas and Electricity Markets (Ofgem) supports GEMA in its day to day work. This decision is made by or on behalf of GEMA.

² This document is notice of the reasons for this decision as required by section 38A of the Gas Act 1986.

³ System Operator Allowed Revenue is the amount the licensee should aim to recover through its NTS System Operation Charges, derived in accordance with the formula in Part C of Special Condition 2.3.

The modification proposal

On 8 September 2023, NGT (The Proposer) raised UNC857 with the expressed aim of reducing year-on-year GNTS charge volatility.

The existing methodology to determine Non-Transmission Services Gas Year Target Revenue only considers the Allowed Revenue for the Formula Year which ends within the Gas Year without taking account of the Allowed Revenue for the following Formula Year.

The modification would amend the methodology to consider both sections of the Formula Years that fall within the relevant Gas Year. It is proposed the Allowed Formula Year Non-Transmission Revenue for Formula Year T_{+1} will be multiplied by a factor which represents NGT's forecast, for Gas Year Y, of the proportion of Non-Transmission Revenue which will be earned in the part of Formula Year T_{+1} which falls within Gas Year Y.

This modification proposal forms part of a wider package of measures proposed by NGT to reduce GNTS charge volatility and prevent the possibility of negative GNTS charges materialising. This included proposing UNC847 which set a minimum GNTS charge. Ofgem approved UNC847 in November 2023⁴.

UNC Panel⁵ recommendation

At the UNC Panel meeting on 15 February 2024, Panel Members considered UNC857 would better facilitate the UNC objectives and Panel voted unanimously to recommend its approval.

Our decision

We have considered the issues raised by the modification proposal and the Final Modification Report (FMR) dated 15 February 2024. We have considered and taken into account the

⁴ UNC847: [UNC847: Authority Decision \(ofgem.gov.uk\)](https://www.ofgem.gov.uk/unc847)

⁵ The UNC Panel is established and constituted from time to time pursuant to and in accordance with the UNC Modification Rules.

responses to the industry consultation(s) on the modification proposal which are attached to the FMR⁶. We have concluded that:

- implementation of the modification proposal will better facilitate the achievement of the relevant methodology objectives of the UNC;⁷ and
- directing that the modification be made is consistent with our principal objective and statutory duties.⁸

Reasons for our decision

We consider this modification proposal will better facilitate UNC Relevant Code Objective (RO) (d) and UNC Charging Methodology Relevant Objectives (CMRO) (b) and (c).

RO (d), so far as is consistent with sub-paragraphs (a) to (c), the securing of effective competition:

(i) between relevant shippers;

(ii) between relevant suppliers; and/or

(iii) between DN operators (who have entered into transportation arrangements with other relevant gas transporters) and relevant shippers

The Proposer considers the modification will enhance effective competition between Shippers by allowing them a 'greater level of confidence in their forecasts of prospective use of network costs'.⁹ The Proposer notes this will allow Users to set their own service costs 'more accurately' and potentially allow for 'a lower risk margin'.¹⁰

⁶ UNC modification proposals, modification reports and representations can be viewed on the Joint Office of Gas Transporters website at www.gasgovernance.co.uk

⁷ As set out in Standard Special Condition A11(1) of the Gas Transporters Licence, available at: <https://epr.ofgem.gov.uk//Content/Documents/Standard%20Special%20Condition%20-%20PART%20A%20Consolidated%20-%20Current%20Version.pdf>

⁸ The Authority's statutory duties are wider than matters which the Panel must take into consideration and are detailed mainly in the Gas Act 1986 as amended.

⁹ UNC857 Final Modification Report: [Final Modification Report 0857 v2.0 \(Appended Reps\).pdf](http://www.gasgovernance.co.uk) (gasgovernance.co.uk), p13.

¹⁰ FMR, p13.

Panel Members agreed with the Proposer that the modification would further RO (d). However, some Panel Members observed the benefits of the modification in securing effective competition may 'only be marginal'.¹¹ One Workgroup Participant argued it was 'unclear whether this Proposal would reduce uncertainty in the way articulated by the Proposer'¹² while another Participant noted it was difficult to prove the modification would positively enhance competition between Shippers.¹³

We note the responses from Panel Members and Workgroup Participants. We note that no Panel Member or Workgroup Participant argued the Proposal was negative in respect of RO (d). Furthermore, we acknowledge the consultation response¹⁴ which supported implementation and emphasised that volatile prices have significant impacts for Shippers and their risk management practices.

On balance, we consider the modification would have a positive impact on RO (d). The modification is expected to reduce year-on-year volatility in GNTS charges which is partly driven by the misalignment between the Formula Year and the Gas Year. As a result, we expect this modification will provide a more stable and predictable GNTS charge for Users. This increased stability will reduce risks and potentially costs for Users when they come to use forecasts of their network costs and set their service costs for customers. We consider this modification will provide a more level playing field for competition by reducing uncertainty and cost-based barriers to entry. We expect the modification will level the playing field for Users with less resources to absorb risk and forecast their network costs thus facilitating effective competition between Shippers.

A Panel Member considered there was a 'theoretical risk of windfall gains/losses'¹⁵ for Shippers who have entered into long-term contracts depending on the implementation of this modification. We note this observation. However, we acknowledge that Shippers entering long-term contracts will do so in the understanding that the UNC charging methodology may change and will factor this into their risk management processes. Therefore, we do not consider the

¹¹ FMR, p17.

¹² FMR, p13.

¹³ FMR, p14.

¹⁴ UNC857 Representation: [Consultation Template \(gasgovernance.co.uk\)](https://www.gasgovernance.co.uk/consultation-template), p1.

¹⁵ FMR, p17.

theoretical risk of windfall gains/losses will substantially impact certain market participants over others and therefore have a dampening effect on competition. Furthermore, we do not consider this modification will impact competition between suppliers or between DN operators and relevant Shippers.

CMRO (b) that, so far as is consistent with sub-paragraph (a), the charging methodology properly takes account of developments in the transportation business

The Proposer notes the existing methodology had 'worked well'¹⁶ prior to the 2021 gas crisis as Allowed Revenues and corresponding charges had remained 'relatively consistent'. However, with the onset of the wholesale gas crisis, the sudden change in the cost of procuring shrinkage gas resulted in a significant increase in NGT's costs and Allowed Revenues. The misalignment between the Formula Year and Gas Year, the timings of when costs are incurred, and when they are permitted to be included in the Allowed Revenues have since contributed to driving year-on-year GNTS charge volatility. Without intervention, NGT projections suggest this methodology will continue to drive year-on-year GNTS charge volatility.¹⁷

The modification aims to address this issue by amending the methodology to consider both sections of the Formula Year which fall within the Gas Year. We note this approach is similar to UNC796¹⁸ which the Proposer¹⁹ and a Workgroup Participant²⁰ noted was successful in reducing year-on-year volatility in the Capacity Reserve price rate. We thus consider the Proposal to be a pragmatic response to the residual effects of the wholesale gas crisis on the transportation business and that it would therefore have a positive impact on CMRO (b).

A Workgroup Participant noted the Proposal was complex and the calculations under the proposed methodology 'may be difficult for interested parties to replicate for themselves'.²¹ The Proposer agreed the calculations involved were complex and provided a walkthrough of an Excel

¹⁶ FMR, p5.

¹⁷ FMR, p7.

¹⁸ UNC796: [UNC796: Revision to the Determination of National Grid NTS Target Revenue for Transportation Charging \(ofgem.gov.uk\)](https://www.ofgem.gov.uk/unc796-revision-to-the-determination-of-national-grid-nts-target-revenue-for-transportation-charging)

¹⁹ FMR, p7.

²⁰ FMR, p14.

²¹ FMR, p12.

model at December workgroup to demonstrate the mechanism.²² We acknowledge the comments from the Proposer and Workgroup Participants regarding the complexity of the proposal. We expect the Proposer's publication of the updated Non-Transmission Services model and publication of information on inputs which contribute towards the determination of charges will provide interested parties with transparency and act as a mitigation towards this potential risk. Nonetheless, we continue to encourage participants in the modification process to consider whether their proposals are easily replicated by interested parties when developing future.

CMRO (c) that, so far as is consistent with sub-paragraphs (a) and (b), compliance with the charging methodology facilitates effective competition between gas shippers and between gas suppliers

Given the similarity of CMRO (c) and RO (d), we refer back to our previous assessment of RO (d). We consider the modification would have a positive impact on CMRO (c). The modification is expected to reduce year-on-year volatility in GNTS charges which is partly driven by the misalignment between the Formula Year and the Gas Year. As a result, we expect this modification will provide a more stable and predictable GNTS charge for Users. This increased stability will reduce risks and potentially costs for Users when they come to use forecasts of their network costs and set their service costs for customers. We consider this modification will provide a more level playing field for competition by reducing uncertainty and therefore cost-based barriers to entry. We expect the modification will level the playing field for Users with less resources to absorb risk and forecast their network costs thus facilitating effective competition between Shippers.

Our principal objective and statutory duties

The Authority's principal objective is to protect the interests of existing and future consumers in relation to gas conveyed through pipes and electricity conveyed by distribution or transmission systems.

²² Excel model for December workgroup: [General Non-Transmission Charge Model 0857 - NTSCMF.xlsx \(live.com\)](#)

In the FMR, the Proposer argues the modification is expected to deliver a reduction on year-on-year GNTS charge volatility. We have previously noted the proposed modification is similar to the solution employed in UNC796²³ which was successful in reducing year-on-year volatility in the Capacity Reserve Price rate. We therefore agree with the Proposer that the modification is expected to deliver a reduction on year-on-year GNTS charge volatility. Furthermore, we note the comment from the Workgroup Participant that a 'smaller range of volatility might be helpful'²⁴ when Users come to set charges for their customers. We expect a reduction in volatility would enable Users to set their service costs with a lower risk premium - resulting in lower prices for consumers. For this reason, we consider that approving UNC857 is consistent with our principal statutory duty of protecting the interests of consumers.

Decision notice

In accordance with Standard Special Condition A11 of the Gas Transporters licence, the Authority hereby directs that modification proposal UNC857: Revision to the Determination of Non-Transmission Services Gas Year Revenue be made.

William Duff

Head of Gas Systems and Operation

Signed on behalf of the Authority and authorised for that purpose

²³ UNC796: [UNC796: Revision to the Determination of National Grid NTS Target Revenue for Transportation Charging \(ofgem.gov.uk\)](#)

²⁴ FMR, p14.